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CABINET AFFAIRS STAFFING MEMORANDUM

7

Date: 10/05/84 **Number:** 169082CA ~~**Due By:**~~ ---------------

Subject: Cabinet Council on Economic Affairs with the President Tuesday, October 9, 1984 - 2:00 p.m. - Cabinet Room

	Action	FYI
ALL CABINET MEMBERS	☐	☐
Vice President	☑	☐
State	☑	☐
Treasury	☑	☐
Defense	☑	☐
Attorney General	☐	☑
Interior	☐	☑
Agriculture	☑	☐
Commerce	☑	☐
Labor	☑	☐
HHS	☐	☑
HUD	☑	☐
Transportation	☑	☐
Energy	☐	☑
Education	☐	☑
Counsellor	☑	☐
OMB	☑	☐
CIA	☐	☑
UN	☐	☑
USTR	☑	☐
GSA	☐	☐
EPA	☐	☐
NASA	☐	☐
OPM	☐	☐
VA	☐	☐
SBA	☐	☐

	Action	FYI
CEA	☑	☐
CEQ	☐	☐
OSTP	☐	☐
	☐	☐
	☐	☐
	☐	☐
Baker	☑	☐
Deaver	☐	☑
Darman *(For WH Staffing)*	☑	☐
Mc Farlane	☐	☑
Svahn	☑	☐
Chapman	☐	☑
	☐	☐
	☐	☐
	☐	☐
	☐	☐
Executive Secretary for:		
CCCT	☐	☐
CCEA	☑	☐
CCFA	☐	☐
CCHR	☐	☐
CCLP	☐	☐
CCMA	☐	☐
CCNRE	☐	☐

REMARKS:

The Cabinet Council on Economic Affairs will meet with the President on Tuesday, October 9, 1984 at ~~2:00~~ 2:45 p.m. in the Cabinet Room.

The agenda and background papers are attached. Please note that the second and third agenda items are tentative.

cc: 061

STAT

RETURN TO:

☐ Craig L. Fuller
Assistant to the President
for Cabinet Affairs
456-2823 (White House)

☐ Don Clarey
☑ Tom Gibson
☐ Larry Herbolsheimer

Associate Director
Office of Cabinet Affairs
456-2800 (Room 129, OEOB)

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THE WHITE HOUSE

WASHINGTON

October 5, 1984

MEMORANDUM FOR THE CABINET COUNCIL ON ECONOMIC AFFAIRS

FROM: ROGER B. PORTER RBP

SUBJECT: Agenda and Papers for the October 9 Meeting

The agenda and papers for the October 9 meeting of the Cabinet Council on Economic Affairs are attached. The meeting is scheduled for 2:00 p.m. in the Cabinet Room. Attendance is limited to principals only.

The first agenda item is the report of the Vice President's Task Force on the Regulation of Financial Services. A memorandum from the Vice President and the Secretary of the Treasury, who serve as the Chairman and Vice Chairman of the Task Force, summarizing the problems with the current regulatory system and outlining the proposals for reform is attached. A copy of the full Task Force report is available for Council members who would like one through the Office of the Vice President.

The second agenda item is a review of the current recovery in historical perspective. A paper prepared by Bill Niskanen of the Council of Economic Advisers is attached. It compares the current recovery with previous ones emphasizing the strength and composition of this recovery and some associated conditions such as employment, interest rates, and exchange rates. It weaves together two significant elements of the current recovery: the change in our domestic investment conditions and our net foreign investment position.

If time permits, the third agenda item is a review of government spending and the private economy. A paper prepared by Gregory Ballentine examining trends in the composition of government spending and its effects on the private economy is also attached. The paper differentiates government spending for purchases of products and services and government spending that involves transfer payments. It then examines the effects on the private economy of each of these two basic types of government spending.

Attachments

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THE WHITE HOUSE

WASHINGTON

CABINET COUNCIL ON ECONOMIC AFFAIRS

October 9, 1984

2:00 p.m.

Cabinet Room

AGENDA

1. Report of the Vice President's Task Force on the Regulation of Financial Services (CM # 496)

2. The Current Recovery in Historical Perspective (CM # 494)

3. Government Spending and the Private Economy (CM # 495)

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MEMORANDUM Approved For Release 2008/08/20 : CIA-RDP85-01156R000100150004-7

THE VICE PRESIDENT

WASHINGTON

October 9, 1984

MEMORANDUM FOR THE PRESIDENT

FROM: The Task Group on Regulation of Financial Services

SUBJECT: Reorganization of the Federal Financial Regulatory System Proposed by the Task Group on Regulation of Financial Services

The Task Group on Regulation of Financial Services was formed in December of 1982 to review the federal system for regulating financial institutions. Our objective was to propose legislation to make this system more effective and less burdensome. In addition to ourselves as Chairman and Vice Chairman, the members of the Task Group included the Attorney General, the Director of the Office of Management and Budget, the Chairman of the Council of Economic Advisers, the Assistant to the President for Policy Development and the heads of the seven federal financial agencies.[1] The Task Group's Final Report contains 50 separate legislative recommendations that were unanimously approved by the members of the Task Group.

Background

Since the Revolutionary War the states have chartered banks and regulated their practices. During the Civil War, however, President Lincoln created the Office of the Comptroller of the Currency as part of the Treasury Department to oversee the chartering and regulation of a system of national banks. The first Comptroller in 1863 employed a total of 5 clerks and 1 messenger.

In the 121 years since creation of the OCC, American financial markets have grown dramatically in both size and complexity. Today over 50,000 different financial firms hold more than $5 trillion of private funds. At the same time, the federal regulatory establishment has also grown dramatically.

---

[1] These are the Fed, OCC (part of Treasury) and FDIC for banks; FHLBB for savings and loans and other thrift institutions;
(Footnote Continued)

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Today seven federal agencies with 37,000 employees regulate financial firms, with annual fees and expenditures of more than $4 billion. Approximately 7,000 federal employees at 3 agencies are engaged full time in regulating banks alone.

Problems with the System

The growth in the regulatory system has occurred piece by piece, and Congress has never comprehensively reviewed, let alone revised, the system. In recent years various types of problems have developed:

1. Excessive Regulation. Various practices (such as opening new bank offices) are subject to regulatory controls that are unnecessary or could be greatly streamlined. In fact, while regulatory controls have greatly increased over recent years, the number of failed institutions has risen for banks and thrifts.

2. Duplication Among Federal Agencies. There is significant overlap and duplication in the responsibilities of the agencies. For example, 5 agencies handle both securities matters and antitrust issues involving banks and thrifts. Similarly, two agencies regulate state-chartered banks, even though all state chartered banks are equivalent from a regulatory perspective. Finally, a bank with a parent holding company is usually subject to 2 different federal agencies, which can greatly increase regulatory costs. Fragmentation can also impair safety and soundness if responsibility for a particular problem becomes unclear.

3. Competitive Inequities. Regulatory differences often create competitive disadvantages for a particular type of firm. For example, during previous high interest periods, banks and S&Ls were generally prohibited from paying market rates on consumer deposits. Not surprisingly, many deposits were transferred to money market funds that were not under comparable restrictions. Deregulating interest rates solved that particular problem, but similar situations continue to exist.

4. Unnecessary Interference with State Regulatory Programs. Approximately 70% of U.S. banks are state-chartered, although federal insurance has meant that virtually all state-chartered depository institutions also have a federal regulator. Unfortunately federal agencies often duplicate activities performed by the states, even in areas unrelated to maintaining a stable financial system.

(Footnote Continued)
NCUA for credit unions; SEC for securities firms; and the CFTC for commodities and futures trading firms.

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Proposals for Reform

The Task Group recommendations are designed to streamline the overall system and improve agency accountability. The present agencies would continue to exist, but in many areas their authority would be modified.

The specific recommendations of the Task Group are discussed in detail in its Final Report, a copy of which is attached. However, key points include:

Reorganization of Bank Regulatory Agencies

- 3 federal bank regulators would be reduced to 2 by eliminating the FDIC's role in general bank supervision. An upgraded agency within the Treasury Department would regulate all national banks, while the Fed would handle all federal regulation of state-chartered banks.
- The agency regulating a bank would also usually supervise its parent holding company, thus breaking the Fed's current monopoly on regulation of bank holding companies and subjecting most banking organizations to only one federal regulator rather than 2.
- The Fed would continue to supervise the holding companies of the very largest banks and those with significant international activities.
- The FDIC would be recast as an insurance agency rather than an all-purpose regulator to sharpen its ability to protect depositors. A l its current responsibilities for environmental, consumer and other laws not related to the solvency of insured banks would be transferred to other agencies.
- The Fed would transfer its authority to establish the permissible activities of bank holding companies to Treasury, although it would maintain a limited veto right over new activities.

Transfer of Regulatory Authority to the States

- A new program would transfer current federal supervision of many state-chartered banks and S&Ls to the better state regulatory agencies, creating new incentives for states to assume a stronger role in supervision.
- Federal agencies would be directed to assist interested state agencies in upgrading their capabilities to assume full supervision of state-chartered institutions.

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Streamlining of Existing Regulations

- The special regulatory system for thrifts would be maintained, but eligibility would be based on whether an institution is actually competing as a thrift, rather than its type of charter.

- Antitrust and securities matters would each be handled by 1 agency rather than 5.

- Many specific regulatory provisions would be simplified to eliminate unnecessary burden, such as by eliminating permits to open branches or install automatic teller machines.

Recommendation: The Administration should support the specific proposals set forth in the Final Report of the Task Group to reform the federal financial regulatory system. The Vice President's office should continue to coordinate the drafting of specific implementing legislation by the appropriate agencies for submission by the Administration to Congress for priority consideration next year.

Approve ____________________ Disapprove ______________

George Bush
CHAIRMAN

Donald Regan
VICE CHAIRMAN

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COUNCIL OF ECONOMIC ADVISERS
WASHINGTON, D C 20500

~~MARTIN FELDSTEIN, CHAIRMAN~~
WILLIAM A. NISKANEN
WILLIAM POOLE

October 5, 1984

MEMORANDUM FOR THE CABINET COUNCIL ON ECONOMIC AFFAIRS

FROM: WILLIAM A. NISKANEN WAN

SUBJECT: CHARACTERISTICS OF THE CURRENT RECOVERY

The "flash" estimates for GNP in the third quarter, as well as the revised data for the second quarter, indicate a significant deceleration in the rate of economic growth. A comparison of the first seven quarters of this recovery with the "typical" postwar recovery, however, indicates that this recovery is still exceptionally strong.

The attached material -- a set of talking points, graphs, and tables -- compares the current recovery with the typical postwar recovery in four dimensions.

1. The strength and composition of real GNP;

2. the relation of domestic investment and the foreign balances;

3. changes in employment and income conditions, and

4. changes in prices and interest rates.

Note: Data from the GNP accounts for the third quarter of 1984, except real GNP and the deflator, are not public and may not be released. This material will be revised when the preliminary estimates are available later this month and can be released at that time.

Attachments

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STRENGTH AND COMPOSITION OF REAL GNP

- Current recovery is the strongest in 30 years, 20 percent stronger than "typical" recovery.
- Strongest components
  - Business fixed-investment growth is three times as strong as in typical recovery.
  - Change in business inventories is more than twice as strong, and current inventory/sales ratio is still low.
- Normal components
  - Personal consumption expenditures
  - Residential investment
  - Government purchases
- Weak component
  - Import growth nearly five times as strong as in typical recovery.

Note: Current recovery data include data from 1984/III "flash" are not public (except for real GNP), and are not to be released.

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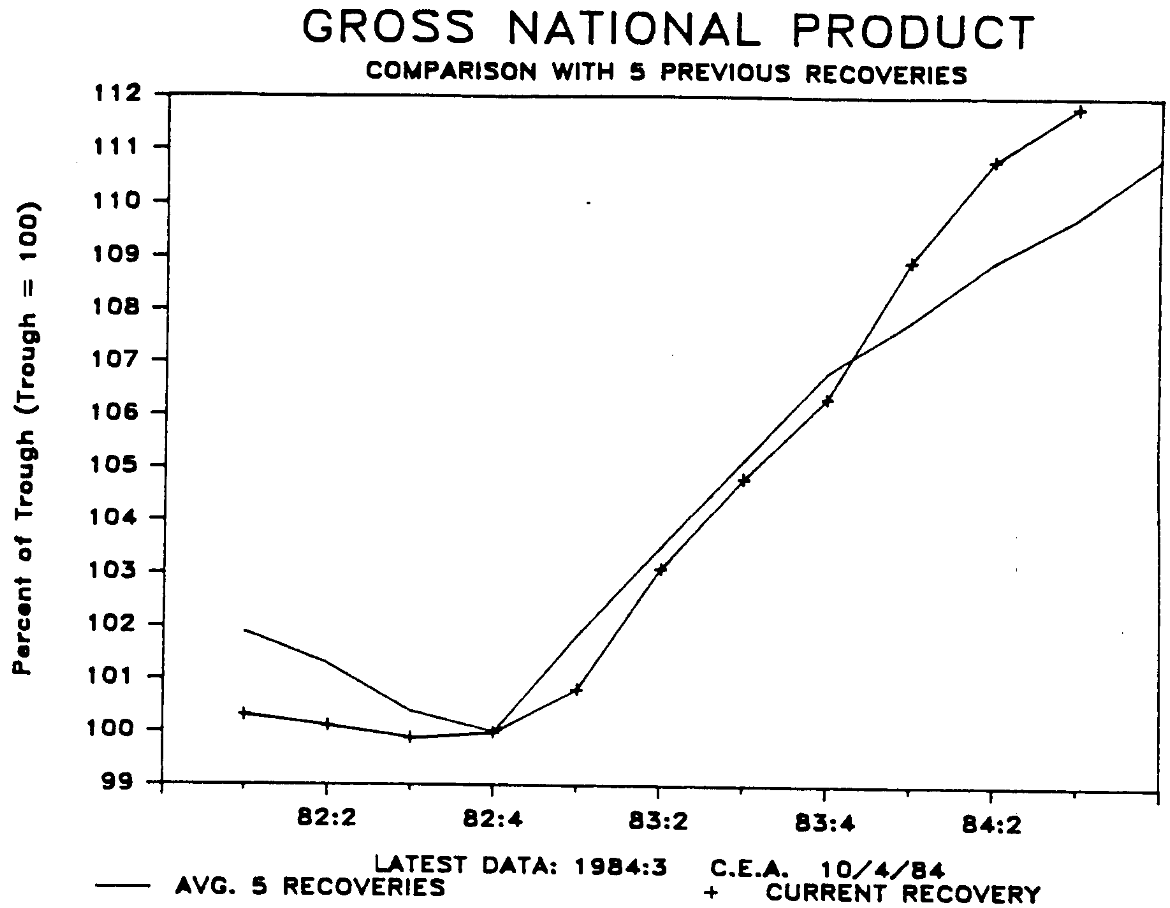

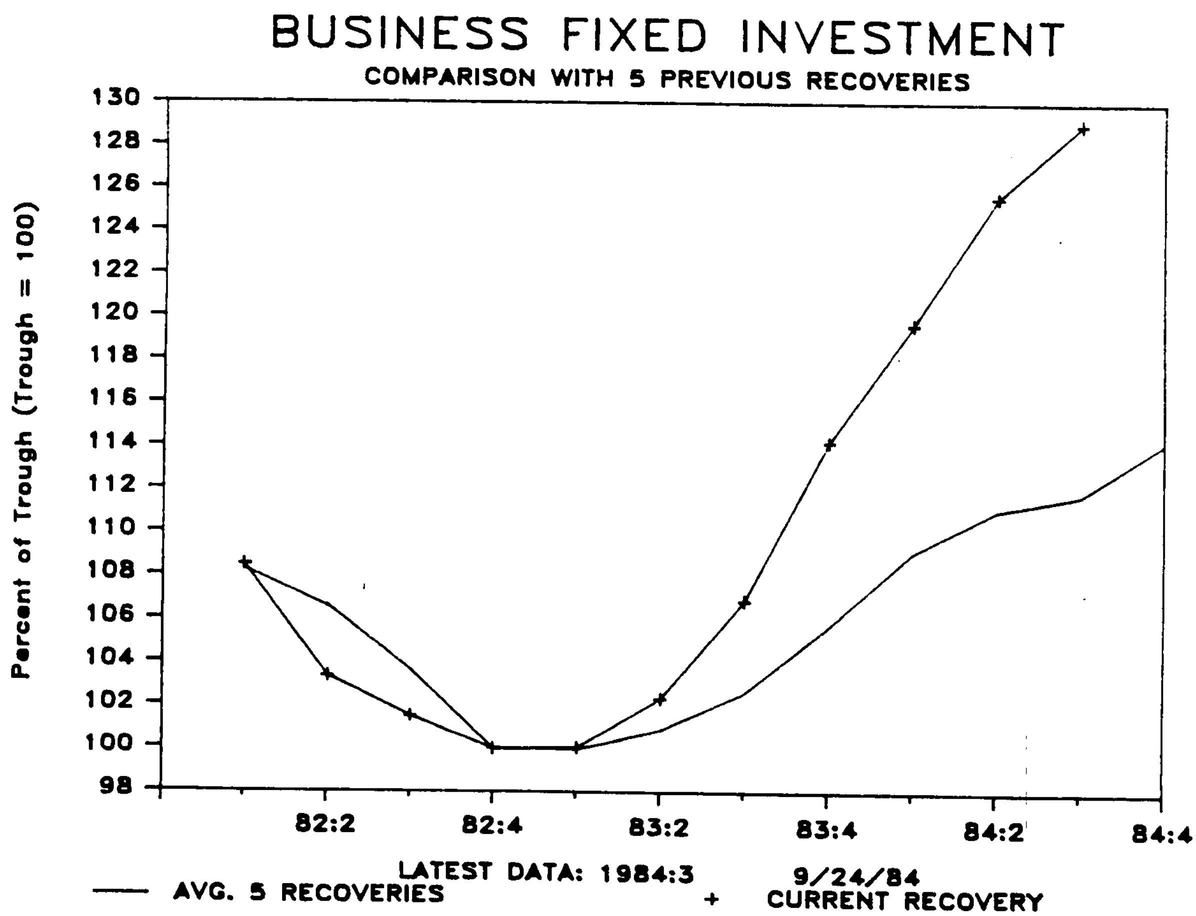

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TABLE 1

Sector Contribution to Growth
"Typical" and Current Recovery

	Annual Rate Over First 7 Quarters	
	Typical 1/	Current 2/
REAL GNP	5.5	6.6
Sector Contributions (percentage points)		
Personal Consumption Expenditures	3.2	3.4
Durables	.9	1.2
Residential	.6	.8
Business Fixed-Investment	.6	1.8
Nonresidential Structures	.1	.3
Producers' Durable Equip.	.5	1.5
Change in Business Inventories	.9	2.1
Net Exports	-.1	-1.7
Exports	.3	.6
Imports	-.5	-2.3
Government	.2	.2
Federal	-.2	.0
State and Local	.4	.2
FINAL SALES	4.5	4.4

1/ Average of recoveries from 1954-II, 1958-II, 1961-I, 1970-IV and 1975-I recession troughs.

2/ Calculated from 1982-IV current recession trough incorporating preliminary "Flash" estimates.

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RELATION OF DOMESTIC INVESTMENT AND FOREIGN BALANCES

- Net foreign investment is equal to the difference between domestic saving and investment.

- Trade actions will not change trade balances, unless they indirectly affect domestic saving and investment.

- U.S. private saving is larger than private investment; the United States could have a current account surplus if government borrowing was zero.

- Increase in trade deficit due to strong increase in private domestic investment relative to increase in net saving.

- Increase in private domestic investment financed by
  - increase in private saving 52%
  - increase in foreign investment in United States 29%
  - reduction in government borrowing 19%

- Other effects of increase in trade deficit
  - increase in output abroad
  - reduction of investment abroad
  - severe strains within U.S. economy

- Important to reduce trade deficit by means that
  - increase private saving
  - reduce government borrowing
  - avoid measures that reduce private investment

Note: 1984/III data are not public and are not to be released.

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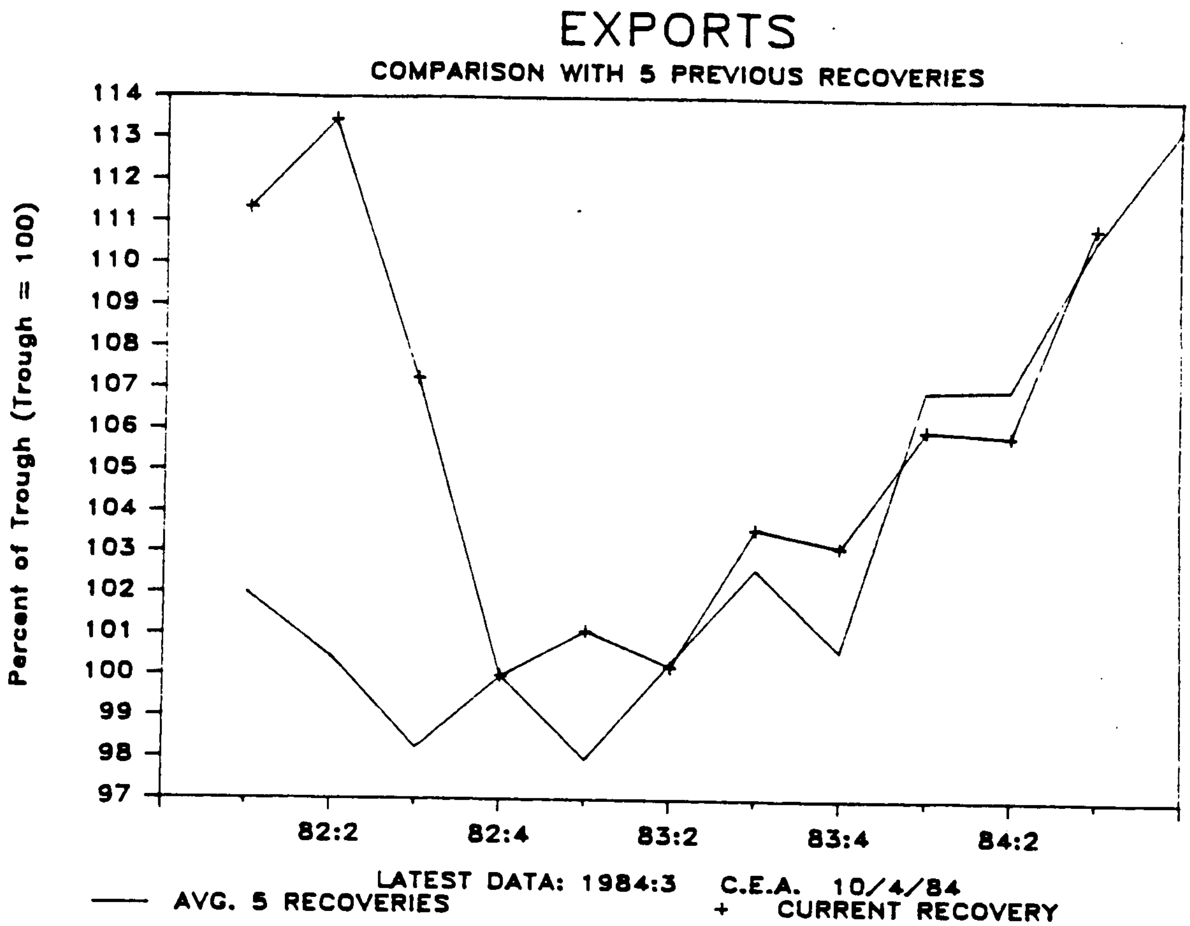

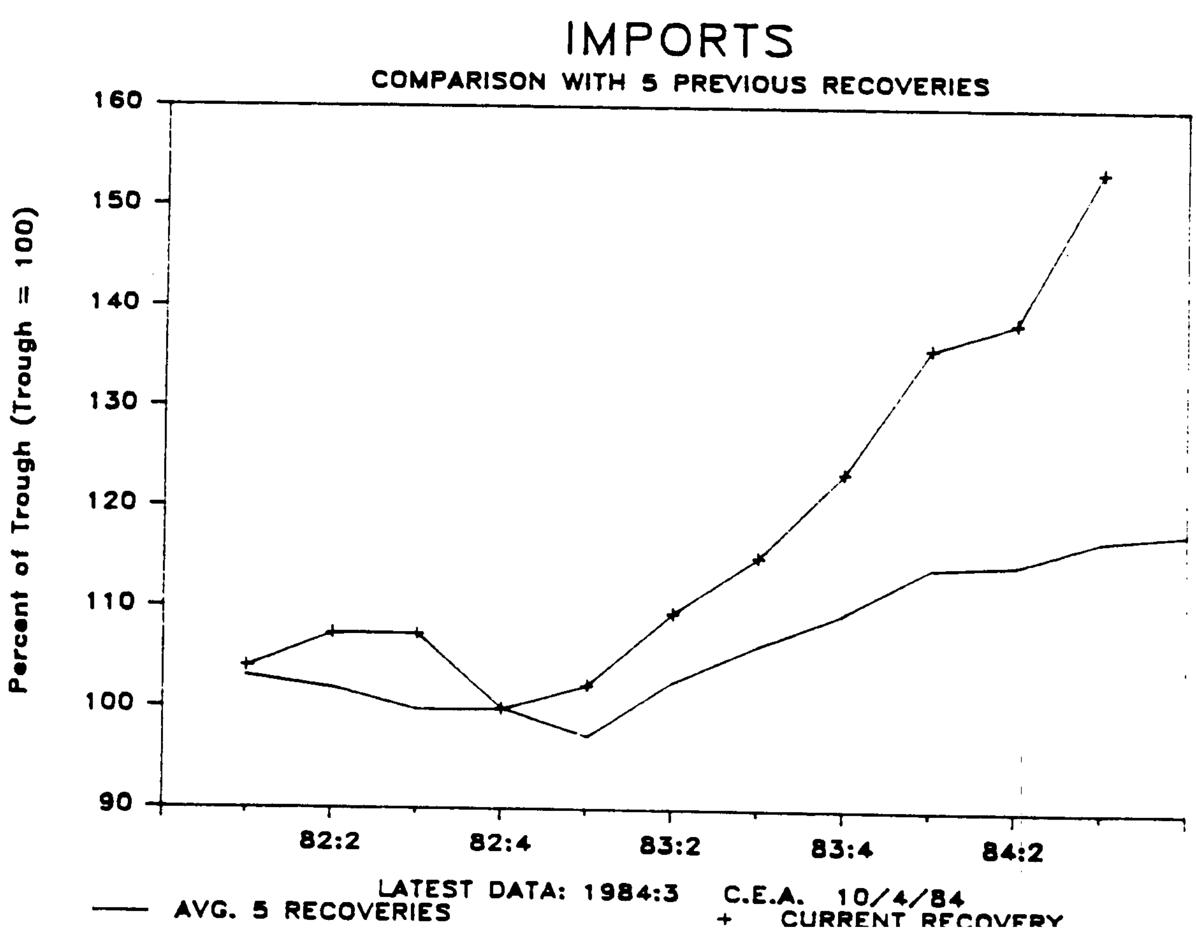

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TABLE 2

Relation of Domestic Investment and Foreign Balances

	Domestic Saving and Investment								Foreign Balances				
	PS	-	GB	-	PI	+	SD	=	T	+	S	=	NFI

(billions of dollars, annual rate)

82/IV	524.0	-	179.2	-	376.2	+	10.5	=	- 43.6	+	22.7	=	- 20.9
84/III	686.1	-	120.2	-	667.5	-	9.0	=	- 127.4	+	16.8	=	- 110.6
Change	162.1	+	59.0	-	291.3	-	19.5	=	- 83.8	-	5.9	=	- 89.7

- **PS** Gross private saving
- **GB** Net government borrowing
- **PI** Gross private domestic investment
- **SD** Statistical discrepancy
- **T** Balance on trade in goods
- **S** Balance on services, interest, and transfers
- **NFI** Net foreign investment

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EMPLOYMENT AND INCOME

- Employment conditions have been much stronger than during typical recovery.

- Total employment has increased at a 3.3 percent annual rate, and total hours worked has increased at an even higher rate.

- The total number of people unemployed, the unemployment rate, and initial claims have all declined at a record peacetime rate.

- Although real gross weekly earnings and real personal income have each increased at a rate slower than in the typical recovery, real personal income less transfers has increased at a record peacetime rate.

- The general improvement in employment and real income conditions in this recovery far exceeds the effects of any specific government measures to increase employment and income.

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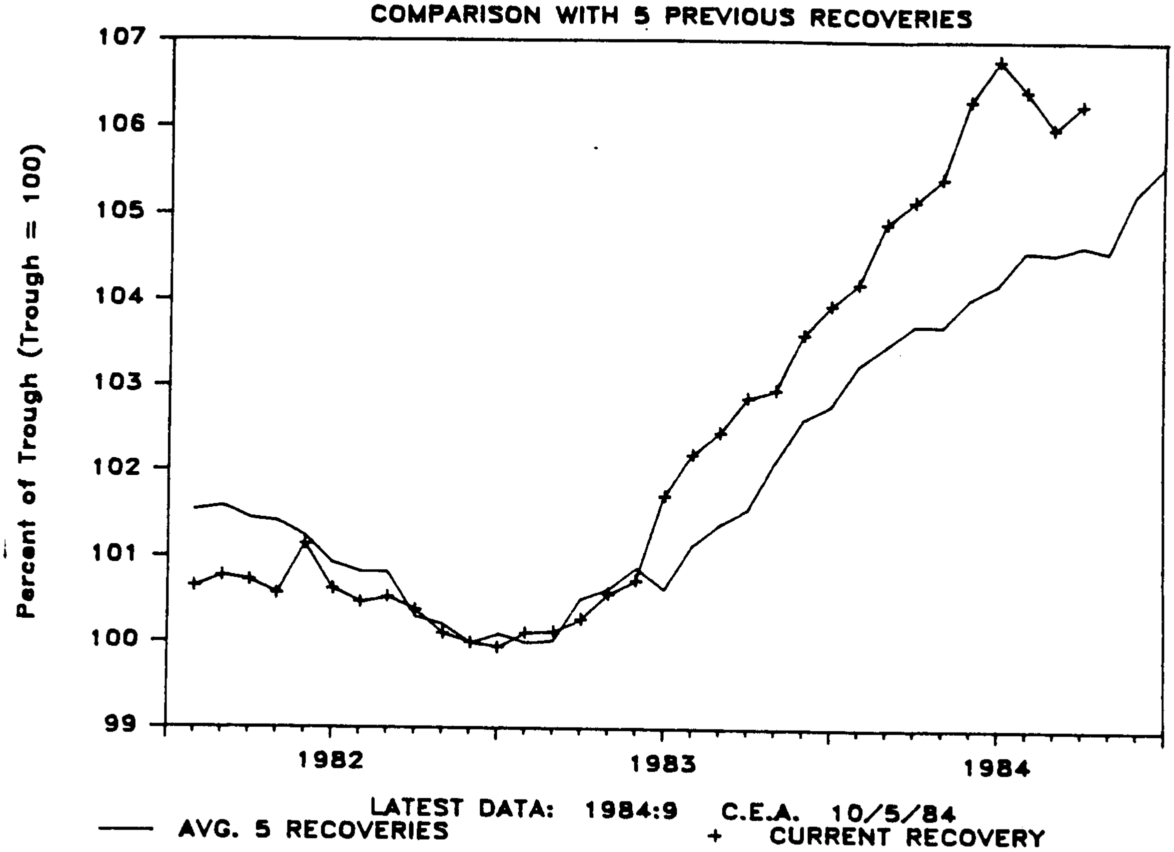
CIVILIAN EMPLOYMENT

COMPARISON WITH 5 PREVIOUS RECOVERIES



UNEMPLOYMENT

COMLARISON WITH 5 PREVIOUS RECOVERIES

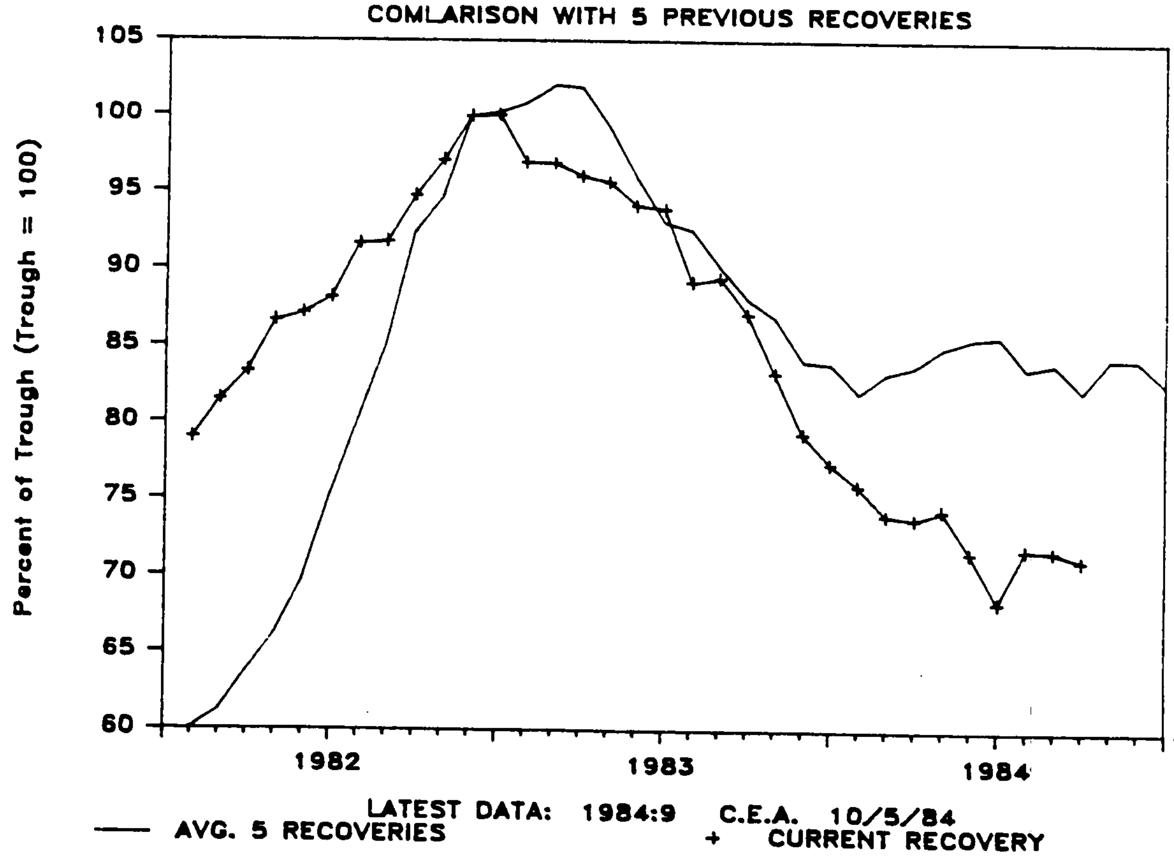


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TABLE 3

EMPLOYMENT AND INCOME -- "TYPICAL" AND CURRENT RECOVERY

	Typical	Current
	(% annual rate)	
Employment Conditions (First 22 Months)		
Total Employment	2.4	3.3
Total Hours Worked	3.3 3/	5.6 3/
Unemployment	-10.4	-16.9
Unemployment Rate 1/	-0.7	-1.8
Initial Claims	-18.5 2/	-26.7 2/
Real Earnings and Income (First 21 Months)		
Gross Weekly Earnings 3/	2.8	1.6
Personal Income	5.2	5.1
Personal Income Less Transfers	5.2	6.1

1/ Percentage point change per year.

2/ 20 Months

3/ 1970 and 1975 recoveries only.

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PRICES AND INTEREST RATES

- Consumer prices have increased at a 3.6 percent annual rate in this recovery, somewhat higher than in the typical recovery but much lower than during any comparable period since 1972.

- Producer prices have increased at a slower rate than during the typical recovery, reflecting in part the effects of the large increase in the exchange value of the dollar.

- Strong dollar will continue to limit U.S. inflation rate for some time.

- Interest rates have increased much more in the current recovery, despite a stable inflation rate, reflecting the strong demand for private investment.

- A reduction in government borrowing is probably necessary to

  - reduce interest rates

  - reduce trade deficit

  - sustain growth of private investment

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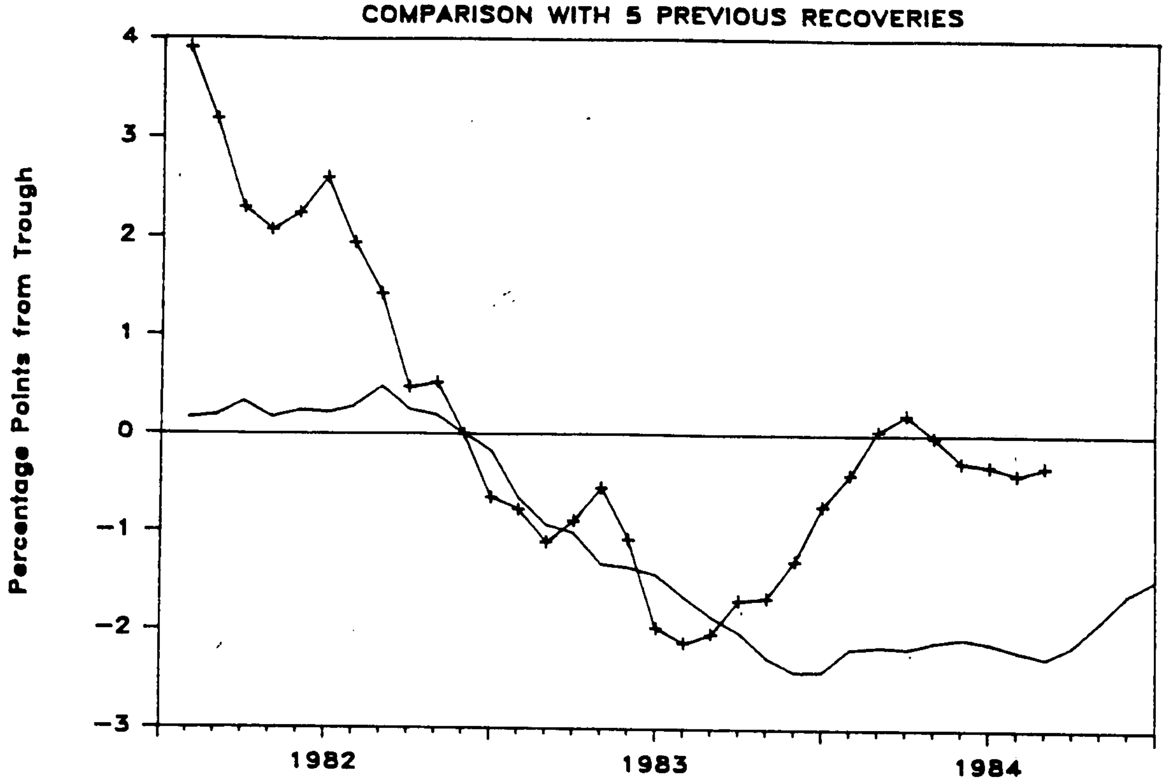
CPI -- % CHANGE FROM YEAR EARLIER

COMPARISON WITH 5 PREVIOUS RECOVERIES

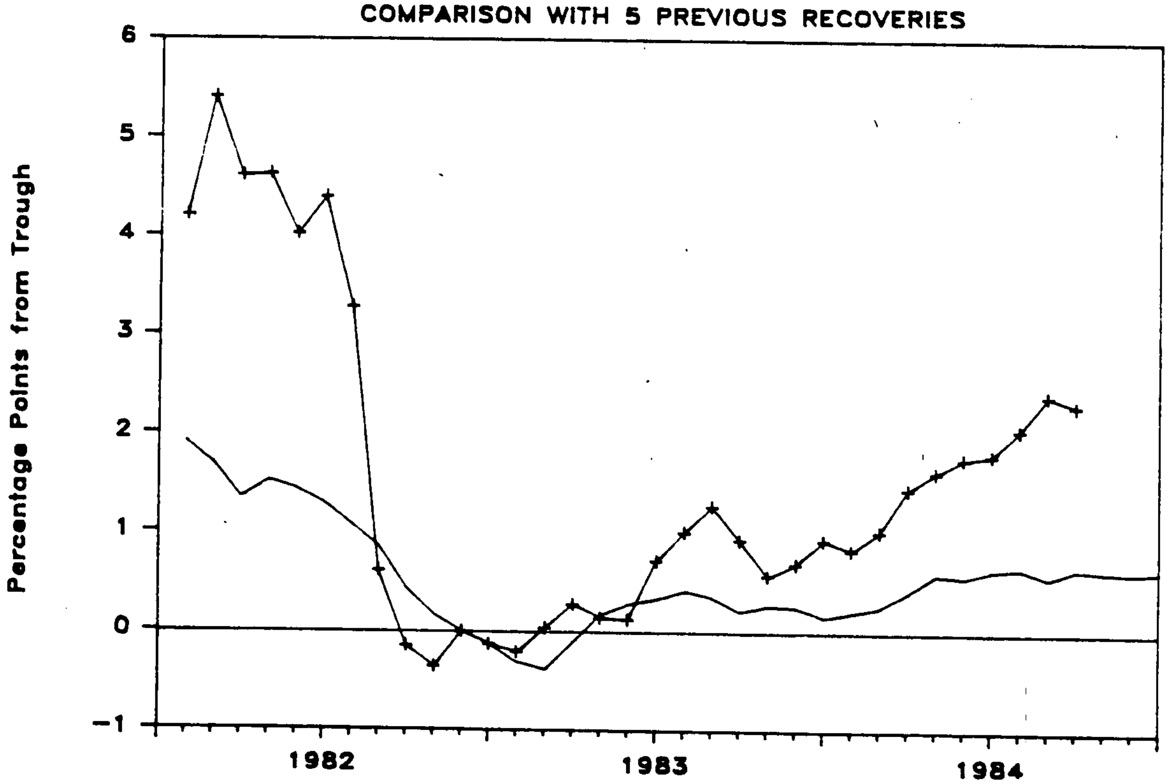


LATEST DATA: 1984:8 C.E.A. 10/5/84

—— AVG. 5 RECOVERIES + CURRENT RECOVERY

TREASURY BILL RATE

COMPARISON WITH 5 PREVIOUS RECOVERIES



LATEST DATA: 1984:9 C.E.A. 10/5/84

—— AVG. 5 RECOVERIES + CURRENT RECOVERY

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TABLE 4

PRICES AND INTEREST RATES - "TYPICAL" AND CURRENT RECOVERY

	Typical	Current
	(% annual rate)	
Price Indices (First 21 Months)		
Consumer Price Index	2.2	3.6
Producer Price Index	1.7	1.4
Interest Rates (First 22 Months) 1/		
Treasury Bill Rate	0.4	1.3
10-Year Bond Rate	0.2	1.1

1/ Percentage point change per year.

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CM #495

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

October 5, 1984

MEMORANDUM FOR THE CABINET COUNCIL ON ECONOMIC AFFAIRS

FROM: J. Gregory Ballentine JGB

SUBJECT: Government Spending and the Private Economy

I. Government Spending and Crowding Out

- o Direct crowding out of the private economy as a whole arises from government spending.
  - -- However, only a portion of government spending crowds out, and
  - -- That portion has been declining relative to GNP since the 1950s.
- o Federal spending consists of two components:
  - -- Purchases of products and services (labor), and
  - -- Transfer payments.
- o Only government purchases of products or services directly shrink (crowd out) private spending. Such purchases crowd out the private economy because, when the government consumes more of the GNP, there is less GNP available for the private economy. For example:
  - -- Persons hired to work in the Federal government are not available to work in the private sector producing private GNP.
  - -- The purchase of equipment (trucks, computers, etc.) by the government directly reduces the amount of such equipment available to the private sector.

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- Government purchases of products and services include:

  - Compensation paid to Defense employees. (23.5% of all purchases of products and services in 1985.)

  - Defense purchases of products and services other than compensation (52%).

  - Compensation paid to all non-Defense Federal employees (including those who administer transfer programs). (10.7%)

  - The cost of all office supplies, office space, cars, etc.

  - The cost of all assets constructed by government such as a spacelab, dams, buildings, etc.

- In contrast, government transfer payments do not directly crowd out the private economy; they transfer purchasing power from one group (taxpayers and others) to another, but that purchasing power is used in the private economy.

- Transfers by the Federal government include:

  - Social Security checks (30.1% of transfers in 1985).

  - Net Interest (19.3%).

  - Medicare (12.0%).

  - The subsidy value of price support payments.

  - Revenue Sharing payments and other grants in aid to State and local governemnts. (These transfers may give rise to State and local purchases of products and services.)

  - The Special Allowance payments for Guaranteed Student Loans.

- Transfer spending does not include the cost of administering transfer programs. Those costs (e.g., payroll, office equipment, etc.) are included in purchases of products or services. Transfers include only the actual dollars passed through the government to those receiving transfers.

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o The table below shows total spending measured on the National Income Accounts basis for 1985 divided between purchases of products and services and transfers.

FY 1985 Federal Spending
($ billions)

Purchases of Products and Services:		
Defense Compensation	$ 79.9	
Other Defense	177.2	
Total Defense Purchases of Products and Services		$257.1
Non-Defense Compensation	36.4	
Other Non-Defense	46.5	
Total Non-Defense Purchases of Products and Services		82.9
TOTAL PURCHASES OF PRODUCTS AND SERVICES		$340.0
Transfers		
Social Security (OASDI)	183.0	
Medicare	72.9	
Unemployment Insurance	18.4	
Federal Retirement (Civilian and Military)	39.8	
SSI	9.9	
Net Interest	117.1	
Grants to State and Local Governments	95.6	
Other	54.3	
TOTAL TRANSFERS		$607.8
TOTAL SPENDING, NIA BASIS		$947.8
TOTAL SPENDING (UNIFIED BUDGET BASIS)		$940.3

o From 1950 until 1980 Federal purchases of products and services have declined as a share of GNP, while transfers have risen. Consequently, direct crowding out of the private economy as a whole by Federal spending is near a postwar low.

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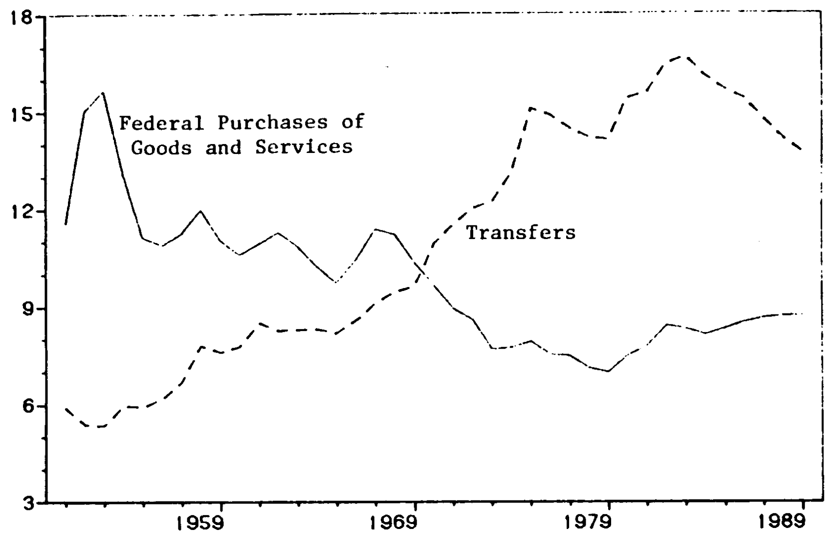
FEDERAL PURCHASES OF GOODS AND SERVICES
AND TRANSFERS
AS A PERCENT OF GNP



o The decline in purchases of products and services is largely due to a decline in defense spending.

	Purchases of Products and Services (% of GNP)	Defense Purchases of Products and Services (% of GNP)	Other Purchases of Products and Services (% of GNP)	Transfers (% of GNP)	Total Federal Spending (% of GNP)
1950-54	12.4	10.5	1.9	6.1	18.5
1955-60	11.3	9.7	1.6	6.8	18.1
1961-64	10.8	8.6	2.2	8.2	19.0
1965-69	10.6	8.2	2.4	9.0	19.6
1970-74	8.5	6.2	2.3	11.9	20.4
1975-79	7.4	4.9	2.5	14.6	22.0
1980-84	8.0	5.7	2.3	16.1	24.1
1985-89*	8.6	6.9	1.7	14.7	23.3

* Projected.

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o The pattern of declining direct crowding out is also indicated by statistics on Federal employment as a share of total employment.

	Federal Compensation (% of Total Compensation)	Defense Compensation (% of Total Compensation)	Non-Defense Compensation (% of Total Compensation)	Federal Employment (% of Civilian Labor Force)	DoD Civilian & Military Employment (% of Civilian Labor Force)	Non-DoD Employment (% of Civilian Labor Force)
1960-64	7.3	5.6	1.7	7.0	5.1	1.9
1965-69	7.4	5.6	1.8	7.6	5.6	2.0
1970-74	6.9	4.9	2.0	6.1	4.2	2.0
1975-79	5.7	3.7	2.0	4.9	3.1	1.8
1980-83	5.3	3.5	1.8	4.5	2.8	1.7

II. Government Redistribution and the Private Economy

o Though government transfer payments do not directly reduce (crowd out) the private economy as a whole, they do require redistributing private resources from some persons in the private economy to other persons.

o This is seen most clearly in the case of tax finance; those paying the taxes can buy less; those receiving the transfers can buy more.

o Government borrowing for transfers also redistributes resources.

o In the case of borrowing, while no one in the private sector directly perceives themselves as worse off (as they do when they pay a tax), nonetheless, there is a redistribution from some part of the private economy to the recipients of the transfers.

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- One possible mechanism by which such a redistribution may occur is the following:

  -- Absent Federal borrowing, savers would loan to a bank that, in turn, would loan to a businessman who buys private investment goods.

  -- Instead, the government borrows from the saver and either gives the proceeds to a transfer recipient, who spends it, or the government spends it to purchase products or services.

  -- As a result, a purchase of investment goods is not made, while a different purchase is made.

- Such a chain of events by which borrowing reduces a segment of the private economy (particularly investment output) is frequently referred to as "crowding out."

- Other, more complex, mechanisms might occur that result in borrowing reducing noninvestment expenditures instead of investment.

- The issue here is not whether borrowing reduces investment. The point is that borrowing must reduce some part of the private economy. If, for example, borrowing is used to finance a transfer program, then the recipients will have a larger share of the private economy; and some other part of the private economy will have shrunk.

- While deficits must crowd out <u>some</u> part of the private economy, <u>net direct crowding out of the private economy as a whole is caused only by government purchases of products and services</u>.

- The <u>means</u> of financing government (<u>taxes, borrowing, or inflation</u>) do not crowd out the private economy as a whole; they <u>only determine which private purchases are reduced when government spends</u>.

III. Indirect Crowding Out

- Though only government purchases of products and services directly crowd out the private economy, taxes, deficits, and transfers can result in significant indirect crowding out.

- Indirect crowding out can arise from the supply side effects of taxes and transfer programs.

  -- Taxes on labor income may induce workers to work less, thereby reducing total GNP.

  -- Taxes on capital income (interest, dividends, etc.) may reduce saving, thereby reducing the capital stock and future GNP.

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-- Transfers to the unemployed who are able to work may induce the recipients to remain unemployed longer, thereby reducing GNP.

-- Transfers to retirees may induce persons currently employed to save less for their own retirement, thereby reducing the capital stock and future GNP.

- Various studies of the indirect crowding out of tax finance suggest that there is about \$1.25 to \$1.50 less of private GNP for every \$1.00 raised by the government in taxes. Thus, the indirect crowding out is on the order of 25¢ to 50¢ for every \$1 raised in taxes.

- If deficit finance reduces expenditures on investment, it also results in indirect crowding out, since the capital stock and future GNP will be lowered.

IV. Conclusions

- While government spending relative to GNP has grown rapidly, spending that directly crowds out the private economy has been declining (relative to GNP) fairly steadily for more than 30 years.

- The government employs a smaller share of the work force than it has previously and purchases a smaller share of GNP than it has previously.

- The expansion of government spending that has occurred has involved redistribution of private resources rather than net direct reduction of private resources.

- Such redistribution directly reduces some persons' private expenditures while increasing others', with no direct reduction in the private economy as a whole.

- Indirect crowding out does result because of the reduced incentives to save and work and the reduced capital formation caused by the taxes or borrowing that finances government.

- Thus, government direct crowding out has declined while government redistribution and indirect crowding out has increased.

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